SASKATCHEWAN MINING DEVELOPMENT CORPORATION

1988 ANNUAL REPORT

89-03440/

SASKATCHEWAN MINING DEVELOPMENT CORPORATION

LETTER OF TRANSMITTAL

March 31, 1989

To Her Honour
Sylvia O. Fedoruk, O.C., S.O.M.
Lieutenant Governor of the
Province of Saskatchewan

Madam:

I have the honour to submit herewith the Annual Report of the Saskatchewan Mining Development Corporation for the year ended December 31, 1988, including the consolidated financial statements in the form approved by the Treasury Board, as well as the Auditors' Report.

I have the honour to be, Madam,

Your obedient servant,

Eric Berntson
Minister Responsible
Saskatchewan Mining
Development Corporation

SASKATCHEWAN MINING DEVELOPMENT CORPORATION

BOARD OF DIRECTORS

Wolfgang Wolff, F.C.A., Chairman
Regina

Hon. Eric Berntson
Regina

Hon. Bob Andrew
Regina

Greg Mrazek
Regina

Ian Disbery
Regina

OFFICERS

Greg Mrazek
President

Ian Disbery
Secretary

OFFICE

2400 College Avenue
Regina, Saskatchewan
S4P 1C8

SASKATCHEWAN MINING DEVELOPMENT CORPORATION

CHAIRMAN'S REPORT

The Merger

Early in 1986, Crown Investments Corporation of Saskatchewan (CIC), a Saskatchewan Crown corporation, and Canada Development Investment Corporation (CDIC), a federal Crown corporation, began to explore the possibility of a merger of Saskatchewan Mining Development Corporation (SMDC) and Eldorado Nuclear Limited (Eldorado). The negotiations that followed proved successful, and on February 22, 1988, the Governments of Saskatchewan and Canada signed a Letter of Intent to merge SMDC and Eldorado into a new company that would be one of the largest integrated uranium companies in the world.

Based on independent evaluations of the future value of the assets contributed by each company at December 31, 1987, it was agreed that SMDC would own 61.5% of the new company and 38.5% would be owned by Eldorado. To facilitate future public participation in the new company, each Government agreed to reduce its holdings over the next seven years through public share offerings, private placements and an employee share purchase plan. Certain ownership restrictions would be placed on future share issues, and the specific timing of the offerings would be subject to market forces.

Legislation to allow the merger was enacted by both Governments during the summer of 1988. On October 5, 1988, the final merger agreement was signed, and Cameco - A Canadian Mining & Energy Corporation (Cameco) was formed. As part of the agreement, substantially all operating assets and contracts of SMDC and Eldorado, as well as certain working capital items relating to operations, were transferred to Cameco on October 5. In exchange, Cameco issued common shares and promissory notes to SMDC and Eldorado in amounts proportionate to ownership. On December 29, 1988, Cameco paid the promissory notes held by SMDC and Eldorado, using the proceeds from a private debt issue.

SMDC: The Holding Company

The conversion of SMDC from mining company to financial holding company was completed through a financial restructuring. All short term notes payable were retired, and equity advances originally provided to SMDC by the Heritage Fund were replaced by equity advances from CIC. To eliminate the corporation's exposure to foreign currency fluctuations, all U.S. dollar-denominated long term debt was converted to Canadian dollar debt. The debt was then transferred to CIC for equity advances. These equity advances were subsequently reduced with funds received from Cameco.

Operations Prior to October 5, 1988

Prior to the merger, SMDC held a 50% interest in the Key Lake uranium mine, a 20% interest in the Cluff Lake uranium mine, a 48.75% interest (with 50.75% voting rights) in the Cigar Lake uranium project, and a 33 1/3% interest in the Eagle North uranium development. In addition to these uranium holdings, SMDC held a 50% interest in the Star Lake gold mine.

During 1988, the Key Lake uranium mine produced just over 12 million pounds of uranium oxide (U_3O_8) while the Cluff Lake mine produced about 2.2 million pounds of U_3O_8. Approximately 35,000 ounces of gold bullion were poured at Star Lake. The Star Lake orebody has been mined out and the ore was stockpiled on the surface to provide feed to the mill. The Cigar Lake test mine phase started with the construction of a headframe, a waste water treatment pond, and expanded surface facilities.

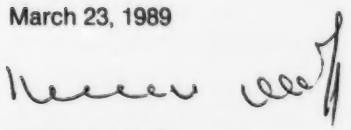
Encouraging results from surface diamond drilling led to two underground gold exploration projects at Fork Lakes, 5 kilometers southwest of the Star Lake mine, and at Laurel Lake in the Flin Flon-Creighton area. In 1988, SMDC discovered copper and zinc deposits at Hanson Lake in northern Saskatchewan and at the Marg project in the Yukon Territory.

Financial Results for 1988

During 1988, SMDC reported net income from all sources of $254.8 million. For accounting purposes, Cameco was deemed to be a continuation of SMDC, thus SMDC recorded the consideration received for the sale of assets at an amount equal to the carrying value of the assets at the time of sale. As a result of the issue of shares by Cameco to purchase the Eldorado assets at fair market value, SMDC recognized an accounting gain of $206 million. SMDC also recorded $16.5 million of income as its share of Cameco's net earnings between October 5 and December 31, and $9.2 million of interest earned on the Cameco promissory note. Income from operations prior to the merger on October 5 was $23.1 million. Due to a change in the Cameco accounting policy for deferred exploration expenses, SMDC charged $163.3 million to reinvested earnings. A dividend of $40 million was declared, compared with $30 million for 1987. This represents the seventh consecutive year that SMDC has declared a dividend. As a result of these transactions, reinvested earnings have increased from $64.3 million, as disclosed in the 1987 Annual Report, to $115.8 million at the end of 1988.

I would like to thank the previous Board of Directors and the SMDC employees for their dedicated service, resulting in a most successful year for the corporation.

March 23, 1989



Wolfgang Wolff
Chairman

AUDITORS' REPORT

To the Members of the Legislative Assembly,
Province of Saskatchewan

We have examined the consolidated statement of financial position of Saskatchewan Mining Development Corporation as at December 31, 1988 and the consolidated statements of operations and reinvested earnings and cash flows for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the Corporation as at December 31, 1988 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied, after giving retroactive effect to the change in the method of accounting for exploration costs as described in Note 6 to the financial statements, on a basis consistent with that of the preceding year.

Clarkson Gordon

Saskatoon, Canada
March 10, 1989

Chartered Accountants

SASKATCHEWAN MINING DEVELOPMENT CORPORATION

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

December 31, 1988

	Note	1988	1987
		(thousands of dollars)	
ASSETS			
			(Note 6)
Current:			
Cash and short-term deposits		$ -	$ 53,607
Accounts receivable		-	29,640
Inventories		-	24,408
Prepaid expenses		-	360
		-	108,015
Investment in Cameco	3	522,465	-
Property, plant and equipment		-	639,835
Deferred financing costs		-	2,923
		$ 522,465	$ 750,773
LIABILITIES AND PROVINCE'S EQUITY			
Current:			
Notes and loans payable		$ -	$ 85,790
Accounts payable and accrued charges		474	47,244
Deferred revenue		-	6,707
Dividend payable		-	30,000
Current portion of long-term debt		-	100,907
		474	270,648
Provision for restoration costs		-	4,061
Deferred revenue and foreign exchange gains		-	6,905
Long-term debt	4	-	318,329
		474	599,943
Province of Saskatchewan's Equity:			
Equity advances	5	406,187	249,841
Reinvested earnings (deficit)	6	115,804	(99,011)
		521,991	150,830
		$ 522,465	$ 750,773

(See accompanying notes)

SASKATCHEWAN MINING DEVELOPMENT CORPORATION

CONSOLIDATED STATEMENT OF OPERATIONS AND REINVESTED EARNINGS

Year ended December 31, 1988

	Note	1988	1987
		(thousands of dollars)	
			(Note 6)
Revenue:			
Uranium concentrates		$ 105,264	$ 186,434
Gold bullion		7,145	8,184
Gain on sale of mineral property		-	7,150
		112,409	201,768
Expenses:			
Operating		24,957	37,065
Depreciation and amortization		32,539	50,545
Interest	7	10,290	34,839
Selling, administrative and other		21,501	19,702
		89,287	142,151
Earnings before sale of assets to Cameco		23,122	59,617
Share of earnings of Cameco	3	16,493	-
Interest earned on Cameco promissory note	3	9,161	-
Earnings before extraordinary item		48,776	59,617
Gain on issue of shares by Cameco	3	206,039	-
Net earnings		254,815	59,617
Reinvested earnings, beginning of year as previously reported		64,267	33,988
Effect of change in accounting policy	6	(163,278)	(162,616)
Reinvested earnings, (deficit) beginning of year as restated		(99,011)	(128,628)
		155,804	(69,011)
Dividend		(40,000)	(30,000)
Reinvested earnings, (deficit) end of year		$ 115,804	$ (99,011)

(See accompanying notes)

SASKATCHEWAN MINING DEVELOPMENT CORPORATION

CONSOLIDATED STATEMENT OF CASH FLOWS

Year ended December 31, 1988

	1988	1987
	(thousands of dollars)	
Cash provided by (used in):		(Note 6)
Operating activities:		
Earnings before extraordinary items	$ 48,776	$ 59,617
Add (deduct) non-cash items		
Depreciation, amortization and other	25,597	49,722
Share of earnings of Cameco	(16,493)	-
Gain on sale of mineral property	-	(7,150)
	57,880	102,189
Net change in non-cash working capital balances relating to operations	(33,158)	(16,821)
	24,722	85,368
Investing activities:		
Proceeds on sale of assets to Cameco	825,357	-
Investment in Cameco	(471,707)	-
Fixed asset additions	(36,473)	(34,387)
Proceeds on sale of mineral property	-	7,780
	317,177	(26,607)
Financing activities:		
Long-term debt repaid	(469,747)	(132,211)
Long-term debt proceeds	64,090	-
Equity advances received	375,046	-
Equity advances repaid	(218,700)	-
Notes payable repaid	(73,250)	63,666
Dividends paid	(70,000)	(15,000)
Deferred revenue	(5,245)	(1,118)
Proceeds on sale of borrowed gold	2,505	12,968
Deferred financing costs	(205)	(277)
	(395,506)	(71,972)
Decrease in cash	(53,607)	(13,211)
Cash, beginning of year	53,607	66,818
Cash, end of year	$ -	$ 53,607

(See accompanying notes)

SASKATCHEWAN MINING DEVELOPMENT CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 1988

1. Accounting Policy

Investment in Cameco - A Canadian Mining & Energy Corporation

In 1988 Saskatchewan Mining Development Corporation (SMDC) acquired 61.5% of the outstanding voting common shares of Cameco - A Canadian Mining & Energy Corporation (Cameco). In conjunction with the other shareholder of Cameco, SMDC has agreed to reduce its ownership interest in Cameco through a series of share offerings over the next seven years. As a result of this formal disposal plan, SMDC has adopted the equity method of accounting for its investment in Cameco. Accordingly, the carrying value of SMDC's investment in Cameco will be adjusted for SMDC's share of Cameco's earnings or losses and reduced by dividends received.

2. Status of Saskatchewan Mining Development Corporation

The Corporation was established by Order-in-Council #865/74 dated June 4, 1974 and continued under the Saskatchewan Mining Development Corporation Act, 1977. The Corporation's accounts are included in the annual consolidated financial statements of Crown Investments Corporation of Saskatchewan (CIC).

3. Investment in Cameco

a) On October 5, 1988, SMDC entered into an agreement with Cameco whereby substantially all of SMDC's operating assets were sold to Cameco. Consideration given to SMDC was in the form of common shares and promissory notes of Cameco and based on the estimated fair market value of the assets sold. Also on October 5, 1988, Cameco purchased substantially all of the operating assets of Eldorado Nuclear Ltd. (ENL) for consideration of promissory notes and common shares of Cameco. As a result of the foregoing transactions, SMDC owned 61.5% of the outstanding voting common shares of Cameco and ENL owned 38.5% as at December 31, 1988.

b) Cameco has accounted for the SMDC-ENL business combination using the purchase method of accounting and has identified SMDC as the purchaser and ENL as the acquired company. The application of this method of accounting results in SMDC's assets and operations being transferred to Cameco on a continuity of interest basis where the amounts are recorded in Cameco at the same carrying values previously used by SMDC. Similarly, SMDC has recorded the consideration received from Cameco at amounts equal to the carrying value of the assets transferred to Cameco.

Details of the assets transferred to Cameco by SMDC (before adjustment for the change in accounting policy - see Note 6) are as follows:

	(thousands of dollars)
Net assets transferred (at book value):	
Current assets	$ 46,776
Property, plant and equipment	806,802
Liabilities assumed by Cameco	(23,097)
Total net assets transferred	$ 830,481
Consideration received (at estimated fair values):	
6,150,000 Cameco common shares	$ 755,600
Cameco promissory note	358,774
Total consideration received	$ 1,114,374

c) In addition, SMDC received one Class B share of Cameco for consideration of $1,000. This share provides SMDC with the ability to exercise special voting rights with respect to the location of Cameco's head office.

d) The net assets acquired by Cameco from ENL were recorded by Cameco at fair market value. The issue of shares to ENL by Cameco and the recording of assets purchased at fair market value resulted in a gain for SMDC, on dilution, of $206 million.

e) On December 29, 1988, SMDC received cash of $370 million from Cameco, representing a principal payment on the promissory note plus accrued interest.

4. Long-Term Debt

During 1988, SMDC entered into a number of cross currency swap transactions whereby its United States dollar debt owing to the Consolidated Fund and related unamortized foreign exchange gains were swapped into Canadian dollar obligations. Subsequent to the swaps, SMDC received an equity advance from CIC in an amount equal to the Canadian dollar obligations resulting from the swaps. SMDC used the equity advances from CIC to repay its Canadian dollar obligations to the Consolidated Fund. On December 15, 1988 the Consolidated Fund provided interest bearing advances to CIC in an amount equal to the Canadian dollar obligations repaid by SMDC.

5. Equity Advances

Equity advances are non-interest bearing and are repayable at the discretion of CIC.

	1988	1987
	(thousands of dollars)	
The Saskatchewan Heritage Fund	$ -	$ 218,700
Crown Investments Corporation of Saskatchewan	406,187	31,141
	$ 406,187	$ 249,841

6. Change in Accounting Policy

During 1988, Cameco adopted the policy of expensing exploration project costs as incurred. Previously, exploration costs had been deferred with the intention that they be amortized by charges against earnings from future mining operations or written off against earnings at such time as it was deemed that a project area did not contain economically recoverable ore reserves. This change in the method of accounting for exploration costs has been applied retroactively by Cameco and accordingly has also been applied retroactively by SMDC. Consequently the 1987 financial statements presented for comparative purposes have been restated. The effect on the 1988 financial statements was to decrease net earnings by $8.5 million (1987-$0.6 million).

In addition, certain 1987 comparative amounts have been restated to conform with the current year's presentation.

7. Interest Expense

	1988	1987
	(thousands of dollars)	
Interest on long-term debt	$ 29,516	$ 61,314
Add amortization of deferred financing costs	1,031	1,589
Less foreign exchange gains	(12,249)	(1,287)
Less interest capitalized and earned	(8,008)	(26,777)
	$ 10,290	$ 34,839

8. Related Parties

Included in these financial statements are expense amounts resulting from routine operating transactions conducted at prevailing market prices with various Saskatchewan Crown controlled departments, agencies and corporations with which the Corporation is related.

Account balances resulting from these transactions are included in the statement of financial position and are settled on normal trade terms.

Other amounts due from related parties and the terms of settlement are described separately in the financial statements and notes thereto.